

# The CPI


## Consumer Price Index:

### What Does it Measure and How?



Do you remember when candy bars cost 50 cents, 25 cents or a nickel? My grandfather does, and chances are if you've spent enough time in the candy aisle you've also noticed the prices of your favorite sweets climbing inexorably skyward! You may have made a similar observation when filling your car with gas, loading it with groceries and heading over to pay that monthly rent check. Have you ever wondered how much the prices of those goods have really changed (lamentations of your progenitors aside)? You're in luck! The Consumer Price Index (CPI), a tool developed by the Bureau of Labor Statistics (BLS), allows you to track the "the average change over time in the prices...of [certain] consumer goods and services." In other words, the CPI is a measure of inflation.

Will the CPI tell you how much the price of your favorite breakfast cereal has fluctuated over the last year? Not exactly, as it would be nearly impossible to track every consumer good and service available (such as every brand of breakfast cereal). Rather than track each and every good and service, the BLS uses what they call a "market basket." The market basket is a collection of goods and services created to represent what the average family or individual typically buys. Information used to create the market basket is collected using Consumer Expenditure Surveys. For these quarterly surveys 7,000 families provide information on their spending habits. An additional



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7,000 families keep diaries detailing everything they bought over a two-week period. The market basket for the current CPI was created using data from 28,000 weekly diaries and 60,000 quarterly diaries collected throughout 2005 and 2006.

The consumer expenditure survey data was used to determine the importance, or weight, of goods and services in the 200-plus categories included in the CPI. Each one of those categories is a part of one of eight major groups including: food and beverages, housing, apparel, transportation, medical care, recreation, education and communication, and other goods and services. Also included are government fees and taxes associated with purchasing goods and services. To further simplify what is included in the market basket, hundreds of representative goods and services are chosen to portray the thousands of varieties available in the marketplace. For example, one specific portion and

brand of breakfast cereal may be used to represent the entire breakfast cereal category. To gather the prices of those representative goods and services, BLS staff call or visit thousands of retail and service outlets to gather the prices of some 80,000 goods monthly. Adjustments are regularly made to account for changes to the quantity, quality, and/or availability of the representative items.

The overall applicability of the market basket to you personally depends on where you live and what you do for a living. CPI measures represent two overlapping population groups.

One is the CPI-U, which reflects the spending patterns of urban consumers and wage earners, as well as clerical workers. The CPI-U covers 87 percent of the total U.S. population. The other is the CPI-W, a subset of the CPI-U, which covers 32 percent of the U.S. population. Neither the CPI-U nor the CPI-W accounts for farm families, people serving in the armed forces, or institutionalized populations (e.g., prisons). Data is also published for certain metropolitan areas (such as Honolulu or Chicago) throughout the year.

A lot of work goes into creating the CPI, and this short article has only scratched the surface on all there is to know about it. You should now have an idea of how it's generated and how to judge the applicability of its figures to you. To learn more about how the CPI is calculated, what it covers, and its limitations, visit <http://www.bls.gov/CPI/>. 